ENERCHEM INTERNATIONAL INC.

The chemistry of quality people, quality products, quality service

2004

Enerchem International Inc. is a manufacturer and distributor of specialty chemicals and hydrocarbon fluids providing solutions to oil and gas processing and production problems and provides energy marketing services. The Company's common shares trade on the Toronto Stock Exchange under the symbol "ECH".

Our Mission Statement

Enerchem strives to provide our cutomers with premium products, outstanding service and superior technical expertise in a safe and environmentally conscientious manner, while enhancing value to our shareholders. Our employees are committed to providing a culture that is based on sound business ethics, integrity, trust and core values that exceed industry standards.

Contents

Annual General Meeting

The Annual General Meeting of the Shareholders will be held on
Thursday, May 19, 2005 at 2:00 p.m.
At the Calgary Petroleum Club, President's Room
3519 – 5th Avenue S.W.
Calgary, Alberta, Canada

All shareholders are cordially invited to attend.

ENERCHEM
INTERNATIONAL INC.

Financial Highlights

Results of Operations

For the years ended December 31	2004	2003
	$	$
Revenues	80,832,614	49,910,680
Net earnings (loss)		
Continuing operations	1,960,700	(362,050)
Discontinued operations	-	(163,874)
Net earnings (loss) for the year	1,960,700	(525,924)
Basic earnings (loss) per share		
Continuing operations	0.14	(0.03)
Discontinued operations	-	(0.01)
Net earnings (loss) per share basic	0.14	(0.04)
Diluted earnings (loss) per share		
Continuing operations	0.13	(0.03)
Discontinued operations	-	(0.01)
Net earnings (loss) per share diluted	0.13	(0.04)
EBITDA (1)	5,509,295	2,108,730
EBITDA per share (2)	0.38	0.15

Financial Position

Total assets	61,653,226	52,168,157
Working capital (3)	11,432,960	6,974,655
Total long-term financial liabilities (4)	3,042,634	1,972,766
Shareholders' equity	39,206,314	36,255,526
Number of shares		
Outstanding, end of year	14,594,610	14,317,655
Average, during the year (5)	14,396,811	14,241,760

(1) represents earnings before interest, taxes, depreciation, amortization and accretion expense
(2) calculated as EBITDA divided by the basic weighted average number of shares outstanding during the year.
(3) calculated as current assets less current liabilities
(4) excludes current portion of long-term debt and obligations under capital leases
(5) represents the weighted basic average number of shares outstanding during the year

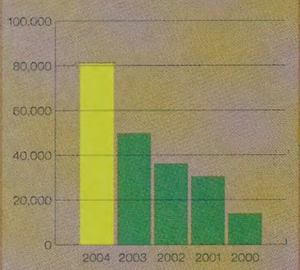
President's Message

To Our Shareholders,

The past year has been one of significant improvement over the results achieved in 2003. Due to successful restructuring initiatives undertaken in the second half of 2003, and continued changes to the way we do business in 2004, I am pleased to report a highly successful and profitable year.

Continued high commodity prices throughout 2004 resulted in record drilling activity in Western Canada and, consequently, unprecedented demand for our products. However, a prolonged spring break-up and unseasonably wet weather during the second and third quarters slowed the pace of drilling somewhat. In addition, as an end user of crude oil in the manufacture of our hydrocarbon and specialty products, we experienced higher feedstock costs during the year which forced us to increase our prices at various times during the year.

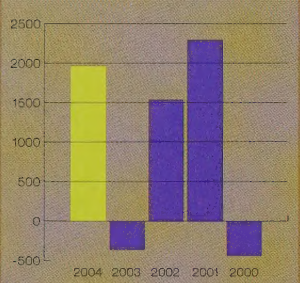
Total Revenues (in $ thousands)



Changing to Maximize Value

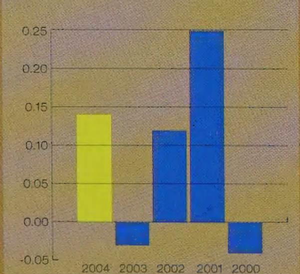
We made two major changes to our corporate structure in 2004. Firstly, in the second quarter of 2004, we created the Energy Marketing Group to manage our feedstock requirements and maximize the value of our hydrocarbon by-product opportunities. As a purchaser of crude oil, we realized that we lacked the necessary experience and expertise to negotiate our feedstock purchase requirements and to maximize value for the by-products resulting from our manufacturing process. These by-products represent the heavy and light streams of crude oil that result from the fractionation process, which Enerchem has historically sold to third-party oil marketing companies. We intend to terminate these present arrangements by the second quarter of 2005. A new tank farm in Slave Lake will allow us to take control of the by-products and sell them through our Energy Marketing Group, thereby realizing substantial increased value for our by-products. Secondly, in the third quarter we streamlined marketing efforts, consolidated administrative procedures and increased our focus on quality control.

Net Earnings (in $ thousands)



One of our major challenges is obtaining enough crude of the right quality to manufacture our products. To this end, we have identified new sources of virgin crude oil which will allow us to maximize the efficiency of our plants in the coming months.

Earnings per share (in $)



As well, we will establish a new facility to clean and recycle our flowback fluids. Flowback is the Fracsol® fracing fluid which Enerchem buys back from its customers after it has been used in the fracturing process. The fluid must be cleaned to remove sediment and water and neutralized to avoid unwanted chemical reactions that could impair the productivity of the well. Enerchem has developed a more efficient and cost-effective method of processing flowback which will result in a significant reduction in crude oil procurement and production costs.

In the second quarter of 2004, we introduced an improved solvent line and reintroduced our Drillsol Plus® drilling fluid in the third quarter. By year end, our drilling fluid sales volumes increased by 122% over the prior year. Our drilling fluid product line exceeds the minimum product guidelines as defined by Industry Recommended Practice 14, and has proven to substantially reduce drilling time when compared to diesel and water; the most commonly used drilling fluids.

All of these activities resulted in significantly improved financial results. Revenues for the year ended December 31, 2004 increased 62% to $80,833,000 from $49,911,000 in 2003. Earnings from continuing operations improved to $1,961,000 in 2004 compared to a net loss from continuing operations of $362,000 in 2003. Earnings per share for the year increased to $0.14 from a net loss per share of $0.03 in 2003. Net cash flows from continuing operations amounted to $3,114,000, an increase of 86% over the prior year.

Outlook

Industry experts anticipate that the Western Canadian oil patch will experience record levels of drilling activity, and have forecasted the number of wells drilled to reach 24,000 in 2005. As well, continued high prices for both WTI and natural gas and strong stock performances are expected into 2006.

Given this outlook, Enerchem anticipates a substantial increase in the demand for all of its product lines over those experienced in 2004 and we anticipate continued improvement in the financial performance of the Company in 2005.

Acknowledgements

I would like to thank our Board of Directors for their continued guidance, our employees for their dedication and innovation and our shareholders for their continued support.

Douglas F. Robinson
President and Chief Executive Officer

Pictured from left to right are:

Robert Satchwell,
Senior Executive,
Engineering & Plant Operations;

Steven R. Houghton,
Senior Executive,
Operations;

J. Barrie Brookman,
Vice President,
Corporate Development;

Douglas F. Robinson,
President &
Chief Executive Officer;

Brian Zubach,
Chief Financial Officer;

Chad Randal,
Senior Executive,
Energy Marketing;

Doug Hildebrandt,
Senior Executive,
Sales and Marketing

Sundre Plant

Illustrated above are the two towers and side strippers of the Sundre plant which are capable of processing 280 m3 per day of feedstock dedicated to the production of Drillsol® and Fracsol®. This plant is capable of processing 340 m³ per day with the use of another tower that produces a variety of solvents. This facility has a finished product storage capacity of 1,400 m³.

Review of Operations

This is Who We Are

Enerchem's operations are divided into two distinct business segments: Oilfield Services, which represents the manufacture and sale of hydrocarbon fluids and specialty chemicals; and Energy Marketing, which represents the purchasing, gathering and marketing of crude oil for resale to refiners and other customers.

Oilfield Services

Products

Enerchem is a provider of hydrocarbon fluids and specialty chemicals ("specialty fluids") that are designed to resolve oilfield processing and production problems. From our blend plant located in Nisku, Alberta and fractionation facilities located in Sundre and Slave Lake, Alberta we manufacture 18 proprietary product lines and more than 300 oil and gas-based formulations which are distributed throughout the Western Canadian Sedimentary Basin through our network of sales and service representatives.

With years of experience behind us, we've developed a wide range of specialty fluids designed to provide technologically advanced solutions to meet oil and gas processing and production requirements. Enerchem's proprietary product lines provide cost effective solutions to a wide variety of oilfield operations which include conventional and heavy oil production, natural gas processing, pipelines, compressor stations and resolve down-hole and surface equipment problems such as internal pipe corrosion and water oil separation.

Enerchem has a specialized focus on trouble shooting and resolving oil and gas production problems. We've developed an industry wide reputation for expertise in:

- Control of paraffin and asphaltene deposition
- Demulsification of hydrocarbon emulsions
- Treatment of work over fluids
- Corrosion control in upstream petroleum production
- Scale control
- Well kill fluids
- Heavy oil diluents
- Sulfur removal fluids

Enerchem holds a unique position in the fracturing fluids marketplace. Our fracturing fluid, Fracsol®, is one of the most widely used fracturing fluids in the hydrocarbon fracturing fluid market. Fracsol® has been recognized by the oil and gas industry as a product providing superior fluid properties with the least amount of production problems.

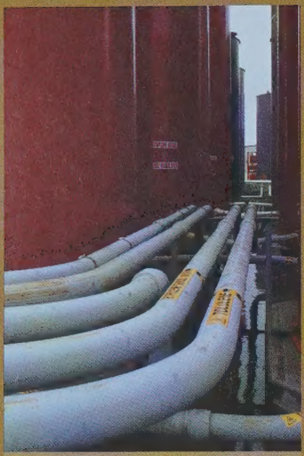
Our premier drilling fluids, Drillsol®, Drillsol Plus®, and Envirosol® were designed to provide cost effective solutions to reducing overall drilling costs, to meet the safety of rig workers and to minimize environmental concerns. Our drilling fluids exceed the minimum product guidelines as defined by Industry Recommended Practice 14 (IRP-14). The IRP-14 specifications were developed by the petroleum industry to minimize health, safety and environmental concerns of products used in oilfield drilling operations.

Facilities

Enerchem's fractionation plants are situated in Slave Lake and Sundre, Alberta and produce our full range of drilling, fracturing and solvent product lines. The Slave Lake facility, completed in 2003, is highly automated and provides three times the production capacity as the Sundre plant. As a manufacturer of hydrocarbon fluids we provide a distinct advantage over similar products supplied by our competitors because our products are designed with a focus on achieving consistency in product specifications and quality. We proudly manufacture our own products right here in Alberta.

Slave Lake plant

Illustrated below, the Slave Lake fractionation plant is capable of processing 800 m3 of crude oil per day and has 5,800 m3 of finished product storage capacity. The facility is located within 1 km of a major highway and has been set up to meet and exceed all environmental and safety requirements. A new feedstock storage tank farm is currently under construction which will allow the Company to better manage feedstock inventories.



Nisku Plant

Illustrated is the piping and pipe racks used to offload raw materials from railcars delivered to the Nisku blend plant's on site railspur. The plant has bulk tank storage capacity in excess of 1 million litres. All of the Company's specialty chemicals are blended from this location.

Enerchem's specialty chemicals are manufactured at our 16,000 sq. ft. blend plant located in Nisku, Alberta. This location houses the Company's chemical blending plant, railcar car siding to procure bulk quantities of base chemical materials, 1 million litre bulk storage tanks and principal warehousing facilities. Enerchem employs strict quality control programs for its specialty chemical products that are designed to test and ensure that all materials used in the formulation of chemical solutions meet stringent product quality specifications. Our quality control program also includes testing of all formulated products before they leave our blending facility in Nisku.

Services

The oil and gas industry in Western Canada has changed dramatically in recent years and in particular from a technical and regulatory compliance perspective. To meet these challenges we listened to our customers and provided solutions with added value benefits.

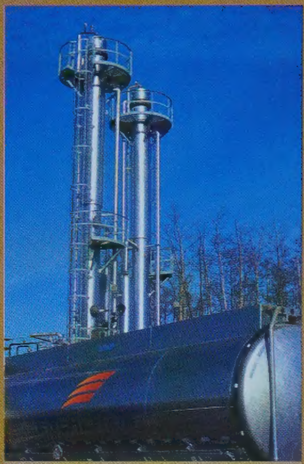
For example, our EnCAM, or Enerchem's Chemical Application Manual, represents a program we implemented to mitigate certain regulatory compliance issues faced by companies affected by regulatory changes relating to oil and gas pipeline systems. Through this program our sales representatives and technical specialists work with the customer to document and maintain on a regular basis all information related to the programs, product selection, monitoring, service reports and studies conducted that are associated with a particular pipeline. This program has been enthusiastically received by our clients' and has been recognized as an important component of pipeline compliance reporting.

When industry demanded safer products, Enerchem changed operating parameters to decrease aromatic components and increase flash points of its hydrocarbon products. When industry demanded more environmentally compatible hydrocarbon based products, Enerchem modified its plant operations to meet health, safety and environmental standards.

Enerchem prides itself on providing rapid response to problems and finding solutions that are innovative and effective. The knowledge, experience and proximity of Enerchem's sales and technical staff are paramount to the success of securing business opportunities. To achieve this capability, Enerchem's network of sales, service and technical representatives are situated in their respective sales territories or key service regions facilitating quick response times to troubleshoot problems and to accommodate high customer call frequency. As an added service to our customers we have established a network of strategically located product distribution centres designed to provide quick product availability to frequently used specialty fluids. For site-specific solutions our laboratory group in Nisku, Alberta is comprised of research and development staff, chemical scientists and technologists dedicated to providing timely and concise results, with domestic critical project turnover times of 24 hours or less.

Energy Marketing

Our expansion into energy marketing activities resulted primarily from recognizing an opportunity to provide increased value to the Company by controlling activities associated with gathering, blending and marketing of our crude oil by-products for resale to refineries or other resellers. Crude oil by-products represent the heavy and light streams of crude oil that result from the fractionation process. In the past, these by-products were sold at discounted values to third party resellers who in turn used their resources to increase by-product value by gathering and blending other grades of crude oil to create a blended crude oil meeting pipeline specifications. This resulted in significant lost opportunities and costs to Enerchem. During 2004 we formally expanded our operations by hiring the necessary expertise and commenced with the process of assessing our activities, requirements and formulating strategies to maximize by-product values, improve our ability to source feedstock for the plants and improve our feedstock purchase arrangements.



Bulk Transportation
We utilize our fleet of bulk hauling vehicles to manage feedstock and finished product deliveries.

International Operations

Enerchem's international presence has been focused on the oil and gas markets of Egypt and North Africa through its investment in the Egyptian Canadian Company for Chemicals Industries F.Z. ("ECC"). Enerchem over the last several years has provided its technical expertise to ECC and has developed a complete line of specialty chemicals to support a state of the art manufacturing and laboratory facility in the Free Zone area of Alexandria, Egypt. This facility, being the first Egyptian engineered and constructed specialty chemicals blending facility in Egypt, employs qualified personnel to meet all the customers product requirements. ECC continues to experience strong growth in its operations.

Health, Safety and Environmental

Enerchem places the importance of safety above all other aspects of the Company's business. Enerchem recognizes that its employees represent its most valuable asset and must be provided with the tools and systems necessary to carry out their work in a safe environment.

We have initiated comprehensive polices and procedures to ensure the health and safety of all our employees, contractors, sub-contractors and visitors.

Enerchem holds a Certificate of Recognition ("COR") for its Oilfield Operations. The COR recognizes that our health and safety management systems meet the Standards of Partnerships developed by Alberta Human Resources and Employment.

We have also implemented programs and guidelines to eliminate our environmental exposures. All environmental laws and regulations are adhered to, including Alberta's Environmental Protection and Enhancement Act, the Canadian Environmental Protection Act, the Transportation of Dangerous Goods Regulations, and the Environmental Operating Guidelines for the Alberta Petroleum Industry.

People – The Best in the Industry

Enerchem's success is the result of the commitment of its people and their dedication to making the customer first. By encouraging growth from within, Enerchem has cultivated an environment that breeds success – technical sales staff, laboratory and engineering staff, dispatch and trucking employees, administrative personnel and skilled operators – working together to timely and effectively meet the requirements of our customers.

Laboratory facilities

Our 3,000 sq. ft. laboratory and research and development centre is located in Nisku, Alberta. Pictured above is an organic halogen analyzer used to detect impurities in hydrocarbon fluids. Our laboratory has state of the art equipment to facilitate product testing and development.

Management's Discussion and Analysis ("MD&A")

The following MD&A focuses on key statistics from the consolidated financial statements and pertains to known risks and uncertainties relating to the oilfield services industry in Western Canada where Enerchem operates. This discussion should not be considered all inclusive, as it excludes changes that may occur in general economic, political and environmental conditions. This discussion and analysis of the financial condition and results of operations for the year ended December 31, 2004 should be read in conjunction with the audited annual consolidated financial statements and related notes and material contained in other parts of this Annual Report and the Company's Annual Information Form. Additional information relating to the Company is available on the System for Electronic Document Analysis and Retrieval ("SEDAR") at www.sedar.com. This MD&A was prepared effective March 2, 2005.

Certain statements contained in this Annual Report, including statements contained in this MD&A, that are not historical facts may be considered "forward looking statements". Forward looking statements are often identified by the use of words such as "seek", "anticipate", "plan", "continue", "estimate", "expect", "may", "will", "project", "potential", "targeting", "intend", "could", "might", "should", "believe", and similar expressions. Such statements are based on current expectations that involve risks and uncertainties which could cause actual results to differ from those anticipated. Important factors that can cause anticipated outcomes to differ materially from actual outcomes include the impact of general economic conditions, industry conditions, competition from other industry participants, volatility of petroleum prices, the ability to attract and retain qualified personnel, changes in laws or regulations, currency fluctuations, continued ability to access capital from available facilities and environmental risks. The Company believes that the expectations reflected in those forward looking statements are reasonable but no assurances can be given that these expectations will prove to be correct and such forward looking statements included in this Annual Report should not be unduly relied upon. These forward looking statements are made as of the date hereof and the Company assumes no obligation to update or revise them to reflect new events or circumstances. References in this MD&A to "Enerchem", "Company", "business", "us", "we", and "our" mean Enerchem International Inc.

Vision, Core Businesses and Strategy

Enerchem strives to provide its customers with premium products, outstanding service and superior technical expertise in a safe and environmentally conscientious manner, while enhancing value to our shareholders.

Business of the Company

Enerchem International Inc. is a provider of specialty chemicals and hydrocarbon fluid solutions ("specialty fluids") designed to resolve oilfield processing and production problems. The Company's specialty fluids provide measurable productivity increases, operating and maintenance cost reductions and solutions to environmental problems. The Company manufactures its proprietary specialty chemical products through its facility located in Nisku, Alberta. Products from this facility provide cost effective solutions to a wide variety of oilfield operations including conventional and heavy oil production, natural gas processing, pipelines, compressor stations and resolve down-hole and surface equipment problems such as internal pipe corrosion and water / oil separation. The Company's proprietary hydrocarbon products are manufactured through its facilities located in Sundre and Slave Lake, Alberta. The Company's fracturing and drilling fluids and solvents are manufactured from these locations. Enerchem's products are marketed and distributed through its network of sales and service representatives. During the third quarter of 2004, the Company diversified its operations with the establishment of its Energy Marketing group. This diversification was precipitated to maximize value received by the Company for its hydrocarbon by-products, provide energy marketing management and expertise and, to mitigate in part, the Company's exposure to the seasonality of its operations. As a result, the Company's activities are divided into two core business segments. The first is Oilfield Services which represents the manufacture and sale of specialty fluids. The second is Energy Marketing which represents the purchasing, gathering and marketing of petroleum for resale to refiners and other customers. The operations of the Company are conducted entirely within the Western Canadian Sedimentary Basin ("WCSB").

The Company's international operations presently represent a 25% investment in an Egyptian company, Egyptian Canadian Company for Chemicals Industries – F.Z., which operates a blend plant in the free zone area of Alexandria, Egypt. Enerchem has invested $750,000 U.S. in this Egyptian company and accounts for its investment on the cost basis as the Company does not exercise significant influence. As a result, earnings from the Company's Egyptian investment are recognized only to the extent received or receivable. During 2003, the Company sold 100% of its wholly owned U.S. subsidiary company, Enerchem International Corporation, which has been reported in the financial statements as discontinued operations.

Business Strategy

Enerchem's distinct advantage is that its facilities, situated in Western Canada, are dedicated to providing a diversified range of proprietary specialty chemicals and hydrocarbon fluids that achieve consistency in product quality to meet oil and gas processing and production requirements common to the WCSB. The Company wants to capitalize on its position and to provide above average returns on investment to its shareholders. To accomplish this, the Company's business strategy is focused on:

- Becoming a low cost producer of quality specialty chemicals and hydrocarbon fluids that provide the best customer value;
- Establishing a more consistent revenue base facilitating stable earnings during seasonal slowdowns in oilfield activity; and
- Optimizing infrastructure and facilities capabilities to capture identified market opportunities and provide competitive advantages.

A substantial component of the Company's future organic growth and profitability is incumbent on its continued ability to successfully market and maximize value received for its hydrocarbon fluid products and by-products. This success hinges on the Company's ability to secure sufficient quantities of crude oil ("feedstock") for its production requirements to meet customer demand and its ability to reflect the underlying value of the Company's products to the retail markets. To accomplish this, the Company's business strategy is focused on:

- Securing favourable long term feedstock arrangements providing opportunity to maximize the Company's production capabilities; and
- Optimizing its business opportunities and operating synergies available through its energy marketing capabilities.

Key Performance Drivers

Enerchem believes the following key performance drivers are critical to the success of the business:

- Hydrocarbon prices which influence the capital expenditure programs and resulting oilfield activity levels of exploration and development companies in the WCSB;
- Weather, which affects the Company's ability to operate in key locations of the WCSB;
- Access to, and retention of, qualified personnel;
- Access to hydrocarbon feedstocks compatible with the Company's plant processing and product quality requirements;
- Expectations of its customers respecting oil and gas exploration and development prospects in the WCSB;
- A continued ability to offer competitive product pricing; and
- Continued access to terminalling facilities required by the Energy Marketing segment to accommodate the purchasing, gathering and marketing of petroleum for resale to refiners and other resellers.

There are several key performance measures the Company uses to monitor and assess its performance relative to the key performance drivers, the implementation of its strategy, and the achievement of its goals and vision.

Some of the Company's key financial performance indicators and results against those indicators are set out below:

Key financial performance indicators

	2004	2003
Consolidated revenue growth	62%	38%
Revenue growth – Oilfield Services segment	32%	38%
Consolidated gross profit percentage	24%	31%
Gross profit percentage – Oilfield Services segment	28%	31%
Net earnings as a percentage of revenues	2.43%	(1.05)%
Basic net earnings per common share	$ 0.14	$ (0.04)
Return on average capital employed (ROACE)	8.3%	0.5%

Return on average capital employed is calculated as the ratio of earnings before income taxes and interest on debt to average capital assets.

In addition, the Company has key operating performance indicators that include but are not limited to: market share, product profitability, product quality and assurance, plant productivity, productivity improvements and waste reduction and operating and administrative cost management.

Capability to Deliver Results

Non-Capital Resources

People are the most critical non-capital resource required in order for the Company to achieve its goals set out in its strategic plan. A formal human resource plan has been implemented in order to ensure the Company focuses on improving and maintaining its employee morale and performance. The Company is continually evaluating its human resource levels to determine if levels are adequate and adequately trained to meet its business requirements. The Company believes that it presently has sufficient human resources to successfully operate its business and to execute its strategic plan.

Capital Resources

The Company has the necessary working capital to meet its current obligations and commitments. The Company maintains a fleet of leased field service vehicles and leased premises which represent its off-balance sheet financing arrangements. During 2004, the Company increased its long term debt by drawing on its available credit facilities with a Canadian chartered bank in order to fund its projects in Grande Prairie and Slave Lake, Alberta. In order to finance future capital expenditure obligations and future growth, Enerchem anticipates obtaining financing through a combination of working capital, cash flow from operations and existing debt facilities. Due to the long term nature of its assets and its historical cost of capital, the Company believes that it must provide an annual 10% to 15% return on average capital employed over the life of its asset base in order to be financially accretive for shareholders and to minimize Enerchem's cost of capital.

Systems and Processes

The Company's operational systems and processes are continuously reviewed by management. During 2004, the Company commenced a review of its compensation system to ensure market competitiveness and to align its human resources to the attainment of the Company's strategic objectives. In addition, several modifications were made with regards to the review and approval processes for capital expenditures, inventory management and electronic communications. The Company is presently evaluating methods and infrastructure requirements to facilitate increased productivity of its fractionation plants in Slave Lake and Sundre and is evaluating processes that will contribute to reduce overall feedstock costs. The foregoing systems and process modifications will align the Company to execute its strategic plan.

Seasonality of Operations

Weather conditions can affect the sale of the Company's products and services. The ability to move heavy equipment in the Canadian oil and natural gas fields is dependent on weather conditions. As a result, spring months in Western Canada and the duration of this "spring break-up" has a direct impact on the Company's activity levels. In addition, many exploration and production areas in the northern WCSB are accessible only in winter months when the ground is frozen hard enough to support the weight of heavy equipment. The timing of freeze up and spring break-up affects the ability to move equipment in and out of these areas. As a result, late March through May is traditionally the Company's slowest period.

Trends and Outlook

Industry analysts anticipate that the total wells drilled in the next two years will remain at or near record levels, or decline moderately, from the number of wells drilled in 2004. Industry analysts are predicting that oil and gas prices will average $40 U.S. per barrel in 2005 and will decline moderately in the following two years, but will remain high by historical standards. The Company believes that long–term fundamentals require continued exploration and production in the WCSB to meet continued North American and worldwide demand for oil and natural gas and as a result expects strong demand for its products and services into 2006.

Selected Annual Information

Selected annual financial information derived from the audited consolidated financial statements for the three most recently completed financial years is set forth below and is prepared in accordance with generally accepted accounting principles in Canada:

For the years ended December 31 (in Canadian dollars)	2004	2003(1)	2002(2)
	$	$	$
Revenues	80,832,614	49,910,680	36,270,819
Net earnings (loss) from continuing operations	1,960,700	(362,050)	1,543,121
Net earnings (loss) per share from continuing operations			
Basic	0.14	(0.03)	0.12
Diluted	0.13	(0.03)	0.12
Net earnings (loss) for the year	1,960,700	(525,924)	1,760,376
Net earnings (loss) per share			
Basic	0.14	(0.04)	0.14
Diluted	0.13	(0.04)	0.13
Total assets	61,653,226	52,168,157	49,685,253
Total long-term financial liabilities	3,042,634	1,972,766	860,652

(1) Restated to reflect stock based compensation expense of $163,300.

(2) Restated to reflect stock based compensation expense of $134,787.

Revenues in 2004 increased by 62% when compared to 2003 and were 123% greater than revenues achieved in 2002. The increase in revenues in 2004 when compared to 2003 and 2002 reflects increased activity levels in the WCSB, increased product revenues from our Oilfield Services segment and increased revenues as a result of the Company's diversification into energy marketing in 2004. On December 1, 2003 the Company sold 100% of its wholly owned U.S. subsidiary company, Enerchem International Corporation. As a result, revenues from its discontinued operations were excluded from consolidated revenues in the amount of $1,166,000 for the year ended December 31, 2003 and $1,141,000 for the year ended December 31, 2002.

The improvement in net earnings from continuing operations for fiscal 2004 when compared to fiscal 2003 largely reflects the affects of increased activity levels in the WCSB and demand for the Company's specialty fluids combined with improved retail product and by-product margins. In addition, during 2004 the Company acheived improved productivity from its Slave Lake plant which resulted in improved product yields and plant utilization when compared to the plant's productivity rates during its first year of operation in 2003.

The Company's total assets have increased steadily since 2002. The increase in total assets in 2004 when compared to 2003 and 2002 reflects the growth experienced by the Company's Oilfield Services segment combined with the added growth in operations provided by the Company's Energy Marketing segment. The Company's long-term liabilities have also increased steadily since 2002. The Company has drawn on its available credit facility with a Canadian chartered bank to finance major capital expenditures incurred by the Company.

Discontinued Operations

On December 1, 2003 the Company sold 100% of the issued and outstanding shares of its wholly owned U.S subsidiary, Enerchem International Corporation, for $530,000. The net gain on the sale of the discontinued operations amounted to $104,000. Details of this divestiture are provided in the notes to the audited consolidated financial statements under note 3, "Discontinued operations."

Results of Continuing Operations

Consolidated Revenues

Consolidated revenues increased by 62% to $80,833,000 for the year ended December 31, 2004 from consolidated revenues of $49,911,000 for the year ended December 31, 2003. During 2004 oilfield activity in the WCSB reached record levels as high prices for oil and natural gas stimulated exploration, drilling and production. Oilfield Services revenues were $65,881,000 in 2004 compared to $49,911,000 in 2003. Energy Marketing, which was initiated at the commencement of third quarter 2004, provided revenues of $14,952,000.

Oilfield Services Revenues

The Company's Oilfield Services segment is focused on the manufacturing and selling of specialty chemicals, solvents, fracturing and drilling fluids (specialty fluids). Oilfield Services' products are designed to provide measurable productivity increases, operating and maintenance cost reductions and solutions to environmental problems. The Oilfield Services' manufacturing facilities are situated in Western Canada and are dedicated to providing a diversified range of proprietary specialty fluids and supporting services designed to ensure consistency in product quality to meet oil and gas processing and production requirements common to the WCSB.

Oilfield Services revenues increased by 32% to $65,881,000 or 82% of the Company's total revenues for the year ended December 31, 2004 compared to $49,911,000 or 100% of total revenues in 2003. The increased revenues, while driven by strong activity levels in the WCSB, primarily resulted from the improved utilization and productivity of the Slave Lake plant. The improvement in the plant's productivity increased our ability to meet the growth in demand for the Company's fracturing and drilling fluids. The Slave Lake plant's average product yield improved by 21% in 2004 when compared to 2003. This contributed to the 44% increase in fracturing and drilling fluid volumes sold in 2004 when compared to 2003. Revenues from fracturing and drilling fluids increased by 42% to $36,703,000 in 2004 compared to $25,937,000 in 2003. More specifically, revenues from fracturing fluids increased by 35% in 2004 compared to last year and drilling fluid revenues increased by 103% for the comparative periods. Revenues from specialty chemicals and solvent fluids in 2004 of $23,793,000 remained relatively unchanged from last year's revenues of $23,974,000. While specialty chemical revenues increased by 11% in 2004 when compared to 2003, solvent revenues declined by 11% in 2004 when compared to last year. The growth in specialty chemical revenues in 2004 resulted from increased sales to key regions targeted by the Company. The decline in solvent revenues in 2004 resulted from competitive pressures in a specific region serviced by the Company.

Energy Marketing Revenues

During the third quarter of 2004, the Company diversified its operations with the establishment of its Energy Marketing group. This diversification was precipitated to maximize value received by the Company for its hydrocarbon by-products, provide energy marketing management and expertise and to mitigate, in part, the Company's exposure to the seasonality of its operations. Energy Marketing represents the purchasing, gathering and marketing of petroleum for resale to refiners and other resellers. The Company uses a third party owned terminalling station to gather and blend various grades of crude oil. Gathering and marketing activities involve relatively large volumes of transactions that provide lower margins when compared to the Oilfield Services segment. Gross margins as a percent of revenues from this business segment would normally range 8% to 10%. Energy Marketing revenues were $14,952,000 in 2004 or 18% of consolidated revenues.

Gross Profit

Consolidated gross profit increased by 28% to $19,624,000 in 2004 from $15,285,000 in 2003. As a percentage of total revenues, gross profit was 24% in 2004 compared to 31% in 2003. More specifically, Oilfield Services gross profit was $18,299,000 in 2004 compared with $15,285,000 in 2003, representing a 20% increase in year-over-year gross profit. Oilfield Services gross profit as a percentage of the business segments revenues was 28% in 2004 compared to 31% in 2003. The Energy Marketing segment achieved a gross profit of 9% in 2004. The decline in total gross margin as a percent of total revenues in 2004 when compared to 2003 can be attributed to the effects of higher crude oil prices and the Energy Marketing segment's activities, which can be largely characterized as high volume but low margin. Record levels of activity in the WCSB have, as indicated earlier, created record demand for the Company's fracturing and drilling fluids. This demand precipitated a steady shift in the Company's product revenue mix as fracturing and drilling fluid revenues comprised 56% of Oilfield Services revenues for 2004 compared to 52% of Oilfield Services revenues in 2003. This shift in product mix combined with the Company's Energy Marketing activities has, however, increased the Company's sensitivity to the volatility in crude oil prices. While the Energy Marketing segment has the flexibility to optimize profit margins whether a strong or weak market exists, Oilfield Services product margins applicable to fracturing and drilling fluids are sensitive to competitive product pressures which can restrict our ability to effect price adjustments.

Operating Expenses

Salaries and employee benefits increased by $367,000 to $7,217,000 in 2004 from $6,850,000 in 2003, representing an increase of 5%. The increase in salary costs on a comparative period basis was partially attributed to increased selling activities. In addition, during the year the Company retroactively adopted the requirements of the Canadian Institute of Chartered Accountants' (CICA) Handbook Section 3870 on stock based compensation, which resulted in the expensing of stock options granted. The impact of expensing the stock options for 2004 was $293,000 and $163,000 for 2003. As a percentage of gross profit, salary costs were 37% in 2004 compared to 45% in 2003.

Selling, general and administration (SG&A) costs increased by $371,000 to $6,971,000 in 2004 representing an increase of 6% over last year's total of $6,600,000. The increase in SG&A expenditures in 2004 can be attributed to general maintenance programs applicable to the operation of the Company's plants and costs associated with increased selling activity levels. As a percentage of gross profit, SG&A costs were 36% in 2004 compared to 43% in 2003.

Depreciation and amortization expense declined by $44,000 to $1,931,000 in 2004 from $1,975,000 in 2003. All of the Company's property, plant and equipment is depreciated or amortized on a declining balance basis. The decline in depreciation and amortization expense in 2004 can be attributed to the year-over-year decline in the pool of assets to which the depreciation and amortization calculations apply. During 2004, the Company adopted the requirements of the CICA Handbook Section 3110, Asset Retirement Obligations ("ARO"), which resulted in the amortization of the initial ARO on adoption of the new standard in the amount of $39,000. In addition, in accordance with the recommendations of this Section, the Company has recorded an accretion expense of $32,000 (refer to notes 1(m) and 8 of the consolidated financial statements). In 2002, the Company adopted the recommendations of the CICA "Revenues and Expenditures During the Pre-Operating Period." In accordance with these recommendations, pre-operating costs incurred during the start-up of the Company's fractionation plant in Slave Lake were capitalized until the plant was capable of consistently providing its intended commercial service. The pre-operating period ended January 1, 2003. As a result these costs are being amortized over a period of five years. The amortization of pre-operating costs in each of 2004 and 2003 totaled $87,000.

Interest expense decreased by $61,000 to $326,000 in 2004 from $387,000 in 2003. Interest expense includes interest costs associated with the Company's use of its operating and term credit facilities and includes interest on capital leases. Interest expense decreased in 2004 as the Company's average outstanding loan balances declined in 2004 when compared to 2003.

Other income decreased by $199,000 to $74,000 in 2004 from $273,000 in 2003. Other income of $320,000 in 2004 reflects one–time revenues earned from non-core business activities, offset by the $275,000 loss on settlement of a legal claim with a former employee.

Enerchem's income tax expense increased proportionately with the increase in profitability. As at December 31, 2004 the Company has approximately $1,478,000 of non-capital losses available to reduce future years' income for tax purposes.

Net Earnings

Net earnings from continuing operations for the year ended December 31, 2004 totaled $1,961,000, representing a $2,323,000 improvement from the results in 2003 which produced a net loss from continuing operations of $362,000. The improved performance in 2004 resulted from improved utilization of the Company's Slave Lake plant, minimized feedstock quality issues, accretive performance by the Energy Marketing segment, and strong growth in Oilfield Services activities. The Company's earnings before interest, taxes, depreciation, amortization and accretion expense (EBITDA) from continuing operations increased by $3,400,000 to $5,509,000 in 2004 from $2,109,000 in 2003.

Summary of Quarterly Results

The following tables provide selected unaudited financial information relating to the Company's quarterly activities in 2004 and 2003 and are prepared in accordance with Canadian generally accepted accounting principles with respect to the preparation of interim financial statements.

2004

Three month period ended (unaudited)

(in Canadian dollars)	December 31	September 30	June 30	March 31
Revenues	30,675,809	22,561,656	8,958,562	18,636,587
Net earnings (loss) from continuing operations	396,405	606,669	(53,987)	1,011,613
Net earnings per share from continuing operations				
Basic	0.03	0.04	-	0.07
Diluted	0.03	0.03	-	0.07
Net earnings (loss) for the period	396,405	606,669	(53,987)	1,011,613
Net earnings (loss) per share for the period				
Basic	0.03	0.04	-	0.07
Diluted	0.03	0.03	-	0.07

2003
Three month period ended (unaudited)

(in Canadian dollars)	December 31	September 30	June 30	March 31
Revenues	13,087,605	11,933,951	10,174,368	14,714,756
Net (loss) earnings from continuing operations	(10,363)	(36,323)	(381,656)	66,292
Net (loss) earnings per share from continuing operations				
Basic	-	-	(0.03)	-
Diluted	-	-	(0.03)	-
Net (loss) earnings for the period	(104,829)	(16,775)	(430,540)	26,220
Net (loss) earnings per share for the period				
Basic	(0.01)	-	(0.03)	-
Diluted	(0.01)	-	(0.03)	-

On a quarter to quarter basis, revenues in 2004 increased in three of four quarters when compared to 2003. This reflects increased activity levels in the WCSB, increased product revenues from its Oilfield Services segment and increased revenues as a result of the Company's diversification into energy marketing in 2004. The trend in quarter to quarter revenues also reflects the seasonality of operations. The Company traditionally experiences increased activity levels during the fall and winter seasons and decreased activity during periods affected by wet or unseasonable weather conditions. Enerchem's hydrocarbon fracturing and drilling fluids are primarily used for deep well drilling and applications common to the foothills region and northern Alberta and British Columbia, areas known for deeper drilling. Oil and gas activity in these geographic regions is normally strong during winter months or when climatic conditions are favourable for such activities.

Liquidity and Capital Resources

Net cash flows from continuing operations for 2004 were $3,114,000 compared to $1,675,000 in 2003, an increase of 86%. The increase in net cash flows was largely driven by the improvement in net earnings in 2004. As at December 31, 2004 the Company had positive working capital of $11,433,000 compared to $6,975,000 at December 31, 2003. This increase in the Company's working capital position is primarily the result of the increased cash flow provided from operations in 2004. The Company's current ratio (defined as current assets divided by current liabilities) was 1.67 to 1 at December 31, 2004 compared to 1.54 to 1 at December 31, 2003. The Company has a bank operating line of credit in the amount of $15,000,000, subject to margining requirements, to finance its working capital requirements. At December 31, 2004, $3,477,000 was drawn by the Company from its available operating line of credit. The Company has a $5,000,000 bank guarantee facility available as security for its feedstock arrangements and purchase commitments. At December 31, 2004 the Company did not have any outstanding bank guarantees. As at the date of this MD&A, the Company is in compliance with all debt covenants and obligations. The terms of the credit facility with the bank provide that non-revolving loans, while repayable on demand by the bank, will not be demanded by the bank unless the Company is in default of its obligations and covenants or if in the opinion of the bank there has been a change in the business, financial condition, operations or conduct of the Company. The Company believes that it has sufficient liquidity to operate its business and to execute its strategic plan.

Net cash used in investing activities from continuing operations was $2,741,000 in 2004 compared to $1,811,000 in 2003. Cash used for investing activities in 2004 related to the purchase of property, plant and equipment which primarily relate to expansion projects in Grande Prairie and Slave Lake, Alberta. Capital expenditures were $3,253,000 in 2004 compared to $2,143,000 in 2003. Capital expenditures during the current year and prior year were funded from operating cash flows and the Company's available credit facilities.

Net cash provided by financing activities was $1,178,000 in 2004 compared to $926,000 in 2003. Proceeds from the issuance of common shares through the Company's employee share purchase plan and upon exercise of stock options were $697,000 in 2004 compared to $749,000 in 2003. At December 31, 2004, the Company had long term debt outstanding of $4,216,000 with scheduled repayments of long-term debt in 2005 in the amount of $1,173,000. The Company used its available long-term credit facilities to finance its expansion projects in Slave Lake and Grande Prairie and to purchase the land and building comprising the obligation under capital lease. The Company's total debt to equity ratio (defined as total liabilities divided by total shareholders' equity) was 0.57 to 1 at December 31, 2004 compared to 0.44 to 1 at December 31, 2003. At December 31, 2004 the Company had available unused revolving and non-revolving long-term credit facilities in the amount of $3,114,000.

Summary of Contractual Obligations and Off-balance Sheet Arrangements

The following table summarizes the Company's contractual obligations including payments due for each of the next five years and thereafter.

Contractual obligations (in Canadian dollars)	Total	Payments due by period Less than 1 year	1 – 3 years	4 – 5 years	After 5 years
Long-term debt (1)	4,215,721	1,173,087	1,657,321	657,386	727,927
Operating leases (2)	891,716	680,956	210,760	-	-
Purchase obligations (3)	600,150	600,150	-	-	-
Total contractual obligations	5,707,587	2,454,193	1,868,081	657,386	727,927

(1) Represents non-revolving bank loans provided through a credit facility with a Canadian chartered bank and are repayable in blended monthly payments of $113,526 and mature at varying dates from May 2006 to May 2020.

(2) Represents normal operating leases comprised of office space and truck fleet.

(3) Represents the Company's commitment to a two year chemical purchase contract effective December 1, 2003 with a U.S. based private company guaranteeing that the Company will purchase chemicals at market prices in amounts no less than $500,000 U.S. ($600,150 CDN) in each year over a two year period.

In the normal course of business with vendors the Company may become contingently liable for performance under letters of guarantee and credit. In this regard, the Company has arranged a $5,000,000 bank guarantee facility available as security for its feedstock arrangements and purchase commitments. At December 31, 2004 the Company did not have any outstanding bank guarantees and letters of credit.

For 2005 the Company expects cash flow from operations and from its sources of financing to be sufficient to meet its contractual obligations and off-balance sheet arrangements.

Share Capital

As at December 31, 2004 the Company had 14,594,610 common shares outstanding. In addition, as at that date the Company has reserved 1,226,000 common shares for issuance under outstanding stock options and up to 182,341 common shares for issuance pursuant to its Employee Share Purchase Plan.

Fourth Quarter

Consolidated Revenues

Consolidated revenues increased by 134% to $30,676,000 for the three months ended December 31, 2004 from consolidated revenues of $13,088,000 for the three months ended December 31, 2003.

Oilfield Services Revenues

Oilfield Services revenues increased by $9,632,000 to $22,719,000 during the quarter compared to $13,088,000 for the same period last year, an increase of 74%. Increased revenues from Oilfield Services were driven by the continued strength in oil and natural gas prices. Revenues from fracturing and drilling fluids increased by 76% to $13,038,000 for the fourth quarter of 2004 compared to $7,394,000 for the same period last year. Revenues from fracturing fluids increased by 49% for the fourth quarter of 2004 when compared to the same quarter in 2003 and drilling fluid revenues increased by 374% for the comparative quarters. Revenues from specialty chemicals and solvent fluids increased by 6% to $6,026,000 for the current quarter from $5,693,000 for the same period last year as a result of continued growth in the northern and central Alberta regions.

Energy Marketing Revenues

Energy Marketing provided revenues of $7,957,000 for the fourth quarter of 2004, an increase of 14% from third quarter 2004 revenues of $6,995,000. Energy Marketing revenues increased due to the overall increase in crude oil prices when compared to the third quarter of 2004 combined with the affects of increased activity levels and by-product volumes available to this business segment. The Company did not have any Energy Marketing operations in 2003.

Gross Profit

Consolidated gross profit increased by 32% to $5,345,000 for the three months ended December 31, 2004 from $4,049,000 when compared to the same period last year. As a percentage of total revenues, gross profit was 17% for the fourth quarter of 2004 compared to 31% for the comparative quarter in 2003. More specifically, Oilfield Services gross profit was $4,690,000 for the fourth quarter of 2004 compared with $4,049,000 for the fourth quarter in 2003. Oilfield Services gross profit as a percentage of the business segments revenues was 21% for the current quarter of 2004 compared to 31% for the same period last year. The Energy Marketing segmented achieved gross profit of 8% for the fourth quarter in 2004. The decline in gross profit for the Oilfield Services segment can be attributed to the affects of the spike up in crude oil prices for the month of October 2004 which represented the business segments most active month for the quarter. Retail prices for the business segments' products for the month of October 2004 were established by the Company and committed to the market in September 2004, and did not anticipate the magnitude of the increase in crude prices.

Operating Expenses

Salaries and employee benefits increased by $237,000, or 14%, to $1,918,000 for the fourth quarter of 2004 from $1,681,000 for the comparative quarter in 2003. The increase in salary costs on a comparative period basis was attributed to profit based bonus payments, stock based compensation expense and increased selling activities. As a percentage of gross profit, salary costs were 36% for the fourth quarter of 2004 compared to 42% for the same quarter in 2003.

Selling, general and administration (SG&A) costs increased by $188,000 to $1,922,000 for the fourth quarter of 2004 representing an increase of 11% over the comparative quarter last year of $1,734,000. The increase in SG&A expenditures for the fourth quarter of 2004 can be attributed to general maintenance programs applicable to the Company's plants and costs associated with increased selling activity levels. As a percentage of gross profit, SG&A costs were 36% for the fourth quarter of 2004 compared to 43% for the same period last year.

Depreciation and amortization expense was $536,000 for the three months ended December 31, 2004 compared to $507,000 for the same period last year. During the fourth quarter of 2004, the Company completed its evaluation of its obligations in accordance with the requirements of CICA Handbook Section 3110, Asset Retirement Obligations (ARO), which resulted in the amortization of the initial ARO on adoption of the new standard in the amount of $39,000. In addition, in accordance with the recommendations of this Section, the Company has recorded an accretion expense of $32,000 (refer to notes 1(m) and 8 of the consolidated financial statements for the year ended December 31, 2004).

Net Earnings

Net earnings from continuing operations for the three months ended December 31, 2004 were $396,000 compared to a net loss from continuing operations of $10,000 for the three months ended December 31, 2003. The improved performance for the fourth quarter of 2004 resulted from improved utilization of the Company's Slave Lake plant, minimized feedstock quality issues, accretive performance by the Energy Marketing segment, and strong growth in Oilfield Services activities. The Company's earnings from continuing operations before interest, taxes, depreciation, amortization and accretion expense (EBITDA) was $1,369,000 for the fourth quarter of 2004 compared to $812,000 for the same quarter last year.

Critical Accounting Policies

The Company's financial statements have been prepared in accordance with Canadian generally accepted accounting principles and include estimates that reflect management's estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and revenue and expenses for the period reported. Estimates are based upon historical experience and various other assumptions that reflect management's best judgments. These estimates are evaluated periodically and form the basis for making judgments regarding the carrying values of assets and liabilities and the reported amount of revenue and expenses. Actual results could differ from these estimates.

The following discussion outlines the accounting policies and practices and management's estimates that are critical to determining Enerchem's financial results.

Goodwill Impairment

The Company tests goodwill for impairment annually and whenever events or circumstances make it more likely than not that an impairment may have occurred, such as a significant adverse change in the business climate or a decision to sell or dispose of a reporting unit. Determining whether impairment has occurred requires valuation of the respective reporting unit, which is estimated using discounted cash flow methodology. When available and as appropriate, comparative market multiples are used to corroborate discounted cash flow results. In applying this methodology, a number of factors are relied upon, including actual operating results, future business plans, economic projections and market data. During the year, management performed its annual evaluation of the carrying value of goodwill and concluded that goodwill of its reporting units was not impaired.

Property, Plant and Equipment

Property, plant and equipment ("PP&E") are recorded at cost and are depreciated over their estimated useful lives on a declining balance basis. Judgment is involved in determining the useful life of the PP&E and the appropriate annual depreciation rate. The Company's investment in PP&E results in depreciation expense being a significant component of operating expenses of the Company and any misjudgment in determining the useful life and annual depreciation rate could result in a misstatement of depreciation expense.

Income Taxes

The provision for income taxes is calculated based on the expected tax treatment of transactions recorded in the Company's consolidated financial statements. Income tax assets and liabilities, both current and future, are measured according to the income tax legislation that is expected to apply when the asset is realized or when the liability settled. If the Company's interpretations differ from those of tax authorities or judgments with respect to tax losses change, the income tax provision could increase or decrease, potentially significantly, in future periods.

Changes in Accounting Policies and Practices

Stock Based Compensation

In October 2003 the CICA amended the accounting standard related to stock based compensation and other stock based payments. The amended section requires recognition of an estimate of the fair value of stock based awards in earnings, rather than allowing note disclosure of pro forma income as if a fair value based method had been used. The Company retroactively adopted the amended standard effective January 1, 2004 with restatement of the 2003 comparative figures. In addition, opening retained earnings have been restated at January 1, 2003 by $134,787 to reflect stock based compensation costs associated with the Company's fiscal year 2002.

Impairment of Long-Lived Assets

Effective January 1, 2004 the Company prospectively adopted the new CICA recommendations in respect of the impairment of long-lived assets. A long-lived asset is an asset that does not meet the definition of a current asset. The new standard requires recognition of an impairment loss when the carrying value of a long-lived asset is not recoverable and exceeds its fair value. Under the standard, an impairment loss is measured as the amount by which the carrying value of the long-lived asset exceeds its fair value.

Asset Retirement Obligations

Effective January 1, 2004, the Company adopted the new CICA recommendations relating to asset retirement obligations, which includes site restoration costs. The new standard requires that obligations associated with the retirement of tangible long-lived assets and associated retirement costs be recognized in the period incurred if a reasonable estimate of fair value can be made. The present value of the estimated asset retirement cost is added to the carrying amount of the related long-lived asset. The depreciation of the capitalized asset retirement cost will be determined on a basis consistent with depreciation of the applicable asset. The asset retirement obligation liability is increased at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the initial fair value measurement. All legal obligations for the retirement of long-lived assets were identified and the fair value of these obligations was determined as of December 2004. The Company has recorded $137,000 as the current fair value of its expected cost as its initial asset retirement obligation ("ARO") on adoption of the new standard. Included in depreciation and amortization of property, plant and equipment is a charge of $39,000 in respect of the amortization of the ARO. In addition, in accordance with the recommendations of this Section, the Company has recorded an accretion expense of $32,000 in the current year.

Hedging Relationships

The CICA issued Accounting Guideline 13 (AcG 13"), "Hedging Relationships", to clarify circumstances in which hedge accounting is appropriate. The guideline requires that all financial instruments that do not qualify as a hedge under the AcG 13, or are not designated as a hedge, be recorded in the balance sheet as either an asset or a liability with changes in fair value recognized in earnings. The Company enters into numerous financial instruments to manage its commodity price risk that do not qualify as hedges under the new accounting guideline. As a result, the Company has elected to not apply hedge accounting to any of its financial instruments.

Consolidation of Variable Interest Entities

In July 2004, the Accounting Standards Board of the CICA announced that, subject to final ballot, it had completed its revisions to Accounting Guideline 15, Consolidation of Variable Interest Entities. This Guideline is virtually identical to FIN 46, a new U.S. standard dealing with the consolidation of these entities. A Variable Interest Entity ("VIE") is an entity that lacks sufficient appropriate equity to finance its activities or whose equity holders lack adequate decision-making ability. Almost any legal structure used to hold assets or conduct activities might be a variable interest entity, including corporations, partnerships, limited liability companies, majority-owned subsidiaries and trusts.

Under the standard, an entity must consolidate a VIE if it holds equity investments, guarantees, subordinated loans, derivatives or other "variable interests" in the VIE that expose the entity to the majority of the VIE's "expected losses". If no one entity has exposure to the majority of expected losses of the VIE, the entity with the majority of its "expected residual returns" must consolidate it.

This new Guideline is effective for annual and interim periods beginning on or after November 1, 2004.

Financial Instruments and Other Instruments

Fair Values

The carrying values of cash, accounts receivable, promissory note, accounts payable, accrued liabilities and bank indebtedness approximate their fair value due to the relatively short periods at maturity on these instruments. The fair value of the Company's long term debt is estimated based on market prices for same or similar instruments and approximates carrying value.

Credit Risk

The Company does not have a significant exposure to any individual customer or other party other than a major international oil & gas company which accounted for 18% of revenue for 2004. Revenues attributable to this customer related to the Company's activities through its Energy Marketing business segment. All amounts collectible from this customer are received within 25 days after the month of delivery of the Company's product. Concentration of credit risk on the Company's trade accounts receivable exists in the oil and gas industry. Management believes that the Company is exposed to minimal credit risk since the majority of its business is conducted with major companies in the industry.

Petroleum Prices

The Company is exposed to changes in petroleum and natural gas prices as a result of its use of petroleum feedstock and natural gas for processing at its Sundre and Slave Lake fractionation plants. The potential fluctuations in petroleum and natural gas prices could have a significant impact on the cost of producing its products and the profitability of the Company. To mitigate the affects on profitability of upward changes in petroleum prices, the Company implements product price increases to reflect their underlying values. This ability, however, is sensitive to competitive product pressures. In addition, this risk is reduced in part, from time to time, through the use of crude oil and natural gas forward purchase contracts. The contracts are not used for speculative trading purposes. Realized gains or losses on these contracts are reported as adjustments to petroleum and natural gas costs in the related production period.

As at December 31, 2004 the Company did not have any outstanding crude oil and natural gas forward purchase contracts. During 2004, the Company had agreements to buy 65,000 barrels of West Texas Intermediate crude oil at strike prices ranging from $41 to $46 CDN per barrel for terms ranging from November 1, 2003 to March 31, 2004. In addition the Company had an agreement to buy 50,000 gigajoules of natural gas at a strike price of $6.25 CDN for the period covering November 1, 2003 to March 31, 2004.

Interest Rate Risk

The Company manages its interest rate risk on borrowings by utilizing a combination of short term fixed rates through the use of 30 to 90 day Banker's Acceptance rates and floating rates on debt. At December 31, 2004 all bank indebtedness represented short term fixed Banker's Acceptances maturing on February 25, 2005.

Health, Safety and Environmental

The Company has achieved and maintained a Certificate of Recognition which is given to employers who develop health and safety programs to meet standards established by the Petroleum Industry Training Service and Alberta Human Resources and Employment. The Company has safety and environmental personnel responsible for maintaining and developing the Company's policies and monitoring the Company's operations to ensure compliance with established policies. However, there can be no assurances that the Company's procedures will prevent environmental damage occurring from spills of materials handled by the Company. The safety and environmental personnel report directly to the President and Chief Executive Officer of the Company.

Competition and Industry Conditions

The capital expenditure programs of oil and gas companies largely affect the services provided by the Company. The magnitude of capital expenditures determines the demand for the Company's services in providing specialty chemical and hydrocarbon fluid solutions to the oil and gas production industry. The primary catalysts to high expenditures and activity levels in the energy industry are oil and gas prices which, in turn, are influenced strongly by supply and demand expectations. The ability to forecast the price of crude oil or natural gas is extremely difficult as many global factors affecting commodity prices are beyond the control of the Company.

There is a strong correlation between drilling activity and demand for the Company's hydrocarbon fracturing and drilling fluids. Industry demand for the Company's fracturing and drilling products is further determined by activity levels that are focused on deep well drilling and applications common to the foothills region and northern Alberta and British Columbia, areas known for deeper drilling. Oil and gas activity in these geographic regions is normally strong during winter months or other times when climatic conditions are favourable. Enerchem's specialty chemical products and services are largely focused on resolving oil and gas production problems encountered on a broader scale throughout the Western Canadian oil and gas market. While the specialty chemicals market offers greater diversity and a more stable revenue stream for our products and services, this market is highly competitive and our revenues and earnings can be affected by our ability to provide effective and economic solutions and by fluctuations in activity levels in our key sales regions. In addition, as our specialty fluids and services are sold in highly competitive markets, the Company's revenues and earnings can be affected by changes in competitive prices.

Operating Risk and Insurance

Enerchem has an insurance and risk management program in place to protect its assets, operations and employees. The Company's operations are, however, subject to risks inherent in the oil and gas industry such as malfunction and failures and natural disasters with resultant fluid spills, explosions and fires. These risks could expose the Company to substantial liability for personal injury, loss of life, business interruption, property damage or destruction, pollution and other environmental damages. Although the Company has obtained insurance against certain of the risks to which it is exposed, such insurance is subject to coverage limits and no assurance can be given that such insurance will be adequate to cover the Company's liabilities or will be generally available in the future or, if available, that premiums will be commercially justifiable. If the Company were to incur substantial liability and such damages were not covered by insurance or were in excess of policy limits, its business, results of operations and financial condition could be materially adversely affected.

Management's Responsibility

The management of Enerchem International Inc. is responsible for the preparation of the accompanying consolidated financial statements and the preparation of all information in the annual report. The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in Canada and are considered by management to present fairly the financial position and operating results of the Company.

The Company maintains various systems of internal control to provide reasonable assurance that transactions are appropriately authorized and recorded, that assets are safeguarded and that financial records are properly maintained to provide accurate and reliable financial statements.

The Board of Directors of the Company carries out its responsibility for the financial statements through its Audit Committee. The Audit Committee has and will meet periodically with the Company's management and independent auditors to review financial reporting matters and internal controls and to review the consolidated financial statements. The Audit Committee reported its findings to the Board of Directors who have approved the consolidated financial statements.

The Company's independent auditors, PricewaterhouseCoopers LLP, Chartered Accountants, have examined the consolidated financial statements whose findings are contained in this annual report

Douglas F. Robinson
President & Chief Executive Officer

Brian M. Zubach
Chief Financial Officer

Auditors' Report

To the Shareholders of
Enerchem International Inc.

We have audited the consolidated balance sheets of Enerchem International Inc. as at December 31, 2004 and 2003 and the consolidated statements of operations, retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2004 and 2003 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants

Edmonton, Canada
February 11, 2005

Consolidated Statement of Operations and Retained Earnings

For the years ended December 31	2004	2003 (restated)
	$	$
Revenues	80,832,614	49,910,680
Cost of sales	61,209,022	34,625,774
Gross profit	19,623,592	15,284,906
Expenses		
Salaries and employee benefits	7,217,455	6,849,881
Selling, general and administration	6,970,554	6,599,553
Depreciation and amortization	1,930,972	1,975,178
Amortization of pre-operating costs	86,871	86,871
Accretion expense (note 8)	32,059	-
Interest expense (note 11)	325,554	386,731
	16,563,465	15,898,214
Earnings (loss) from continuing operations before other income	3,060,127	(613,308)
Other income		
Gain on disposal of property, plant and equipment	29,048	50,356
Loss on settlement of legal claim	(275,344)	-
Rental and other	320,008	222,902
	73,712	273,258
Earnings (loss) from continuing operations before income taxes	3,133,839	(340,050)
Income taxes (note 12)		
Current	-	122,000
Future	1,173,139	(100,000)
	1,173,139	22,000
Net earnings (loss) from continuing operations	1,960,700	(362,050)
Net earnings (loss) from discontinued operations (note 3)	-	(163,874)
Net earnings (loss) for the year	1,960,700	(525,924)
Retained earnings, beginning of period	9,188,212	9,848,923
Implementation of accounting standard (Note 10(c))	-	(134,787)
Retained earnings, restated	9,188,212	9,714,136
Retained earnings, end of period	11,148,912	9,188,212
Basic earnings (loss) per share (note 10(d))		
Continuing operations	0.14	(0.03)
Discontinued operations	-	(0.01)
Net earnings (loss)	0.14	(0.04)
Diluted earnings (loss) per share (note 10(d))		
Continuing operations	0.13	(0.03)
Discontinued operations	-	(0.01)
Net earnings (loss)	0.13	(0.04)
Weighted average shares outstanding (note 10(d))		
Basic	14,396,811	14,241,760
Diluted	14,583,232	14,241,760

Consolidated Balance Sheet

As at December 31	2004	2003
	$	$
Assets		
Current assets		
Cash	2,594,664	1,043,564
Accounts receivable	17,432,270	11,890,868
Inventories	8,039,203	6,316,410
Prepaid expenses and deposits	267,178	493,126
Current portion of promissory note (note 3)	125,964	135,052
	28,459,279	19,879,020
Promissory note (note 3)	188,950	337,630
Other assets (note 6)	1,397,135	1,372,707
Property, plant and equipment (note 4)	25,558,332	24,529,270
Goodwill (note 5)	6,049,530	6,049,530
	61,653,226	52,168,157
Liabilities		
Current liabilities		
Bank indebtedness (note 7)	3,476,944	3,488,605
Accounts payable and accrued liabilities	12,376,288	7,528,458
Income taxes payable	-	137,222
Current portion of obligations under capital leases (note 9)	-	903,515
Current portion of long-term debt (note 7)	1,173,087	846,565
	17,026,319	12,904,365
Long-term debt (note 7)	3,042,634	1,972,766
Asset retirement obligations (note 8)	169,320	-
Future income taxes (note 12)	2,208,639	1,035,500
	22,446,912	15,912,631
Contingent liabilities (note 16)		
Shareholders' equity		
Share capital (note 10)	27,465,971	26,769,227
Contributed surplus (note 10)	591,431	298,087
Retained earnings	11,148,912	9,188,212
	39,206,314	36,255,526
	61,653,226	52,168,157

Signed on behalf of the Board,

LB Phillips

Larry B. Philips
Director

Klein

Kenneth A. Klein
Director

Consolidated Statement of Cash Flows

For the Years ended December 31	2004	2003
	$	$
Operating activities		
Net earnings (loss) from continuing operations	1,960,700	(362,050)
Items not affecting cash -		
Depreciation, amortization and accretion expense	2,043,673	2,062,049
Stock based compensation	293,345	163,300
Gain on disposal of property, plant and equipment	(29,048)	(50,356)
Future income taxes	1,173,139	(100,000)
	5,441,809	1,712,943
Changes in non-cash components of working capital (note 14)	(2,327,639)	(38,362)
Net cash flows provided by continuing operations	3,114,170	1,674,581
Net (loss) from discontinued operations (note 3)	-	(163,874)
Items not affecting cash -		
Depreciation and amortization	-	41,750
Gain on sale of subsidiary company	-	(104,024)
	-	(226,148)
Net change in non-cash components of working capital		145,902
Net cash flows provided by discontinued operations	-	(80,246)
Net cash provided by operating activities	3,114,170	1,594,335
Investing activities		
Purchase of property, plant and equipment	(3,142,069)	(2,016,766)
Decrease (increase) in promissory note	157,768	(472,682)
Proceeds from disposal of property, plant and equipment	354,572	299,846
Proceeds on sale of subsidiary company (note 3)	-	504,749
Increase in other assets	(111,299)	(126,444)
Net cash used in investing activities, continuing operations	(2,741,028)	(1,811,297)
Net cash provided by investing activities, discontinued operations	-	79,727
Net cash used in investing activities	(2,741,028)	(1,731,570)
Financing activities		
Issuance of common shares	696,744	749,369
(Decrease) in bank indebtedness	(11,661)	(2,595,816)
Increase in long-term debt	2,260,978	3,627,455
Repayment of long-term debt	(864,588)	(808,124)
Repayment of obligations under capital leases	(903,515)	(47,137)
Net cash provided by financing activities	1,177,958	925,747
Increase in cash	1,551,100	788,512
Cash - beginning of year	1,043,564	255,052
Cash - end of year	2,594,664	1,043,564

Supplementary information (note 13)

1. Summary of Significant Accounting Policies

(a) Basis of presentation

These financial statements are prepared in accordance with generally accepted accounting principles ("GAAP") in Canada. Prior to December 1, 2003, the financial statements included the accounts of Enerchem International Inc. its wholly owned subsidiary Enerchem International Corporation. The subsidiary company was disposed of on December 1, 2003. Accordingly, operating activities of this subsidiary company have been reported as discontinued operations in the 2003 comparatives and are described in note 3. All significant inter-company transactions have been eliminated.

(b) Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(c) Inventories

Inventories are carried at the lower of average cost and estimated net realizable value. For finished goods inventory, cost includes direct labour and an allocation of overhead that can be attributed to production.

Effective July 1, 2004, the Company changed its method of allocating feedstock costs to its products and by-products that are produced simultaneously in the same processing operation to the relative sales value method. This change coincides with the establishment of the Energy Marketing segment as described in Note 17. Under this method joint product costs are allocated based on each product's percentage of the total sales value of all products produced. This method results in the same gross profit percentage for each joint or common product produced. Under this method revenues from the sale of the Company's by-products are recorded as revenue with the corresponding cost of by-products sold, as determined under the relative sales value method, recorded as a cost of sales. Prior to this change of method, the net realizable value of by-products were applied as a reduction of the main product processing costs. The adoption of this accounting policy was necessitated by the establishment of the Energy Marketing segment and as such has been applied prospectively.

(d) Property, plant and equipment

Property, plant and equipment are recorded at cost and are depreciated over their estimated useful lives on a declining balance basis using the following annual rates:

Buildings	5%
Laboratory equipment	10%
Land improvements	10%
Oilfield equipment	10%
Fractionation processing facilities	5% to 10%
Blend plant facilities	20%
Leasehold improvements	10% to 20%
Automotive equipment	30%
Office, computer equipment and software	20% to 100%

1. Summary of Significant Accounting Policies (continued)

(e) Capital leases

Capital leases are capitalized by recording as assets and liabilities the present value of the payments under the leases. The capitalized value of a depreciable asset under a capital lease is amortized over its estimated useful life on a basis that is consistent with the Company's depreciation policy for similar assets. Lease payments are allocated to a reduction of the obligation and interest expense.

(f) Goodwill

Effective September 1, 2001, the Company adopted the recommendations of Section 3062 of The Canadian Institute of Chartered Accountants (CICA) "Goodwill and Other Intangible Assets." As a result of adopting these recommendations, goodwill with a deemed indefinite life is no longer amortized, but tested for impairment annually, or more frequently, if changes in circumstances indicate a potential impairment.

(g) Investment in foreign operations

The Company's investment in foreign operations is recorded at cost unless there is a decline in value that is other than temporary.

(h) Future income taxes

Income taxes are calculated using the liability method of accounting. Temporary differences arising from the difference between the tax basis of an asset or liability and its carrying amount on the balance sheet are used to calculate future income tax liabilities or assets. Future income tax liabilities or assets are calculated using tax rates anticipated to apply in periods that the temporary differences are expected to reverse. The effect on future income tax liabilities and assets of a change in the tax rate is recognized in income in the period that the change occurs.

(i) Revenue recognition

Revenues are recorded in accordance with the CICA's Emerging Issues Committee Abstract 141 "Revenue Recognition". Revenues associated with sales of the Company's chemical and hydrocarbon fluids are recorded in the period in which the fluids are delivered to the customer, the customer has taken title, assumed the risks and rewards of ownership, amounts are known and collection is reasonably assured.

(j) Earnings per share

Basic earnings per common share are calculated based on the average number of common shares outstanding during the year. Diluted earnings per share are calculated based on the treasury stock method which assumes that any proceeds from the exercise of in the money stock options would be used to purchase the Company's common shares at the average market price during the year. The computation of diluted earnings per share is similar to basic earnings per share except that the weighted average number of shares outstanding is increased to include additional shares from the assumed exercise of stock options, if dilutive.

(k) Stock based compensation

The recommendations of the CICA Handbook Section 3870 "Stock Based Compensation and Other Stock Based Payments" were amended in October 2003 to require the expensing of all stock based compensation awards using a fair value based method of accounting for fiscal years beginning after January 1, 2004. Under the fair value method, compensation expense equal to the fair value of stock options granted is recorded in the statement of operations over the vesting period. Effective January 1, 2004, the Company has retroactively adopted the amended standard with the restatement of the 2003 comparative figures. In addition, opening retained earnings have been restated at January 1, 2003 by $134,787 to reflect stock based compensation costs associated with the Company's fiscal year 2002. The Company has two stock based compensation plans which are described in note 10.

1. Summary of Significant Accounting Policies (continued)

(l) Pre-operating costs

During fiscal 2002, the Company adopted the recommendations of EIC 27 of The Canadian Institute of Chartered Accountants "Revenues and Expenditures During the Pre-Operating Period." In accordance with these recommendations, pre-operating costs incurred during the start-up of the Company's fractionation plant in Slave Lake, Alberta were capitalized until the plant was capable of consistently providing its intended commercial service. Revenues realized from the sale of products produced by the Slave Lake fractionation plant during the pre-operating period were recorded as a reduction of the pre-operating costs. Pre-operating costs are amortized over a period of five years commencing on January 1, 2003.

(m) Asset retirement obligations

Effective January 1, 2004, the Company adopted the recommendations of the CICA Handbook Section 3110, "Asset Retirement Obligations." The new standard requires that obligations associated with the retirement of tangible long-lived assets and associated retirement costs be recognized in the period in which a reasonable estimate of fair value can be made. The standard requires recognition of a liability at a discounted fair value for the future abandonment and restoration associated with the properties. The fair value of the liability is capitalized as part of the cost of the related asset and amortized to expense over its useful life. The liability accretes until the date of expected settlement of the retirement obligation. The related accretion expense is recognized in the statement of operations. The provision will be revised for any changes to timing related to cash flow or undiscounted abandonment costs. Actual expenditures incurred for the purpose of site restoration are charged to the asset retirement obligations to the extent that the liability exists on the balance sheet. Differences between the actual costs incurred and the fair value of the liability recorded are recognized to earnings in the period incurred.

(n) Impairment of long-lived assets

Effective January 1, 2004, the Company adopted the CICA Handbook Section 3063, "Impairment of Long-lived Assets." A long-lived asset is an asset that does not meet the definition of a current asset. This section requires the Company to test long-lived assets to be held and used when events or changes in circumstances occur which may cause their carrying value to exceed the total undiscounted cash flows expected from their use and eventual disposition. An impairment loss, if any, is determined as the excess of the carrying value of the asset over its fair value. This standard was adopted prospectively on January 1, 2004.

2. Financial instruments

(a) Risk management activities

The Company does not have a significant exposure to any individual customer or other party other than a major international oil and gas company which accounted for 18% of revenue for 2004 (2003 – 0%). Revenues attributable to this customer related to the Company's activities through its Energy Marketing business segment. All amounts collectible from this customer are received within 25 days after the month of delivery of the Company's product. Concentration of credit risk on the Company's trade accounts receivable exists in the oil and gas industry. Management believes that the Company is exposed to minimal credit risk since the majority of its business is conducted with major companies in the industry.

The Company is exposed to changes in petroleum and natural gas prices as a result of its use of petroleum feedstock and natural gas for processing at its Sundre and Slave Lake fractionation plants. The potential fluctuations in petroleum and natural gas prices could have a significant impact on the cost of producing its products and the profitability of the Company. This risk is reduced in part, from time to time, through the use of crude oil and natural gas forward purchase contracts. The contracts are not used for speculative trading purposes. Realized gains or losses on these contracts are reported as adjustments to petroleum and natural gas costs in the related production period.

2. Financial instruments (continued)

(a) Risk management activities (continued)

As at December 31, 2004 the Company did not have any outstanding crude oil and natural gas forward purchase contracts. As at December 31, 2003 the Company had agreements to buy 65,000 barrels of West Texas Intermediate crude oil at strike prices ranging from $41 to $46 CDN per barrel for terms ranging from November 1, 2003 to March 31, 2004.

(b) Fair values

The carrying values of cash, accounts receivable, promissory note, accounts payable, accrued liabilities and bank indebtedness approximate their fair value due to the relatively short periods to maturity of these instruments. The fair value of the Company's long term debt is estimated based on market prices for same or similar instruments and approximates carrying value.

(c) Interest rate risk

The Company manages its interest rate risk on borrowings by utilizing a combination of short term fixed rates through the use of 30 to 90 day Banker's Acceptance rates and floating rates on debt. At December 31, 2004 all bank indebtedness was at short term fixed Banker's Acceptance maturing on February 25, 2005.

3. Discontinued operations

On December 1, 2003, the Company sold 100% of the issued and outstanding common shares of its wholly-owned subsidiary, Enerchem International Corporation ("EIC"), for $408,742 U.S. ($530,424 Cdn.) of which $58,930 U.S. ($76,473 Cdn.) was received in cash. The balance of $348,812 U.S. ($452,653 Cdn.) plus a one time carrying charge, represented by a purchaser's promissory note, is receivable in fourty-two monthly installments of $8,745 U.S. ($11,254 Cdn.) each commencing from the date of closing. The promissory note has a deed of trust on land and property, personal guarantees and 65,000 shares of EIC pledged as collateral. The net gain on the sale of discontinued operations amounted to $80,162 U.S. ($104,024 Cdn.) after selling costs of $19,785 U.S. ($25,675 Cdn.). In addition to the foregoing, the Company retained cash and accounts receivable of EIC amounting to $217,887 U.S. ($282,752 Cdn.) and assumed accounts payable amounting to $178,298 U.S. ($231,377 Cdn.) as of the date of closing.

The balance sheet includes the following amounts related to the discontinued operations as at December 31, 2003:

	2003
	$
Assets	
Cash	2,934
Accounts receivable	250,436
Liabilities	
Accounts payable and accrued liabilities	56,616

Revenues and operating activities of this business segment for the eleven months ended November 30, 2003 were as follows:

	2003
	$
Revenues	1,166,197
Inter-segment revenues	1,230,438
	2,396,635
Cost of goods	1,744,477
Gross profit	652,158
Expenses	
Salaries and employee benefits	307,927
Selling, general and administration	288,638
Depreciation and amortization	41,750
Interest expense	3,570
Other expense	179,986
Income taxes	(21,323)
Net (loss) before consolidation adjustments	(148,390)
Consolidation eliminations	(119,508)
Net (loss) from discontinued operations	(267,898)
Gain on sale of subsidiary company	104,024
Net (loss) from discontinued operations	(163,874)

4. Property, plant and equipment

	December 31, 2004			December 31, 2003		
	Cost	Accumulated depreciation	Net	Cost	Accumulated depreciation	Net
	$	$	$	$	$	$
Land	586,198	-	586,198	575,098	-	575,098
Buildings	3,374,536	940,522	2,434,014	2,762,705	605,189	2,157,516
Laboratory equipment	620,486	241,011	379,475	568,841	201,434	367,407
Land improvements	545,469	260,528	284,941	545,469	228,868	316,601
Oilfield equipment	1,462,982	811,414	651,568	1,425,049	741,476	683,573
Fractionation processing facilities	20,487,346	3,505,285	16,982,061	20,479,435	2,666,856	17,812,579
Blend plant facilities	4,895,224	1,617,575	3,277,649	2,930,181	1,282,491	1,647,690
Leasehold improvements	184,797	49,193	135,604	184,797	33,099	151,698
Automotive equipment	1,597,401	1,077,870	519,531	1,536,410	1,041,215	495,195
Office, computer equipment & software	676,554	369,263	307,291	766,053	444,140	321,913
	34,430,993	8,872,661	25,558,332	31,774,038	7,244,768	24,529,270

The above amounts include $nil (December 31, 2003 – $84,800) of land and $nil (December 31, 2003 – $907,195) of buildings under capital leases and related depreciation of $nil (December 31, 2003 – $88,451). The land and building under capital lease were acquired for $875,000 in August 2004 in accordance with the terms of the lease agreement.

Buildings includes $131,425 (December 31, 2003 – $75,049) of costs associated with a warehouse and distribution facility in Grande Prairie and Rocky Mountain House (Slave Lake in 2003) under construction. Fractionation processing facilities includes $1,640,448 (December 31, 2003 - $nil) of costs associated with the construction of storage facilities in Slave Lake. These amounts have not been depreciated as they have not yet been put into use.

5. Goodwill

	December 31, 2004	December 31, 2003
	$	$
Goodwill, beginning of year	6,481,068	6,481,068
Less: accumulated amortization	431,538	431,538
Goodwill, end of year	6,049,530	6,049,530

As described in note 1(f), the Company adopted the recommendations of Section 3062 of The Canadian Institute of Chartered Accountants "Goodwill and Other Intangible Assets". Management has performed its annual evaluation of the carrying value of goodwill and concluded that the goodwill associated with its reporting units was not impaired.

6. Other assets

	December 31, 2004	December 31, 2003
	$	$
Investments - foreign operations	1,114,442	1,014,264
Pre-operating costs	260,613	347,484
Other	22,080	10,959
	1,397,135	1,372,707

At December 31, 2004 accumulated amortization of pre-operating costs is $173,742 (December 31, 2003 $86,871).

6. Other assets (continued)

Investments-foreign operations

Investments-foreign operations represent the Company's investment in its operations in Egypt. During fiscal 1996, the Company entered into an agreement to construct a blend plant in Egypt with Blend Oil Services & Supply. This agreement led to the incorporation of the Egyptian Canadian Company for Chemicals Industries - F.Z., operating in the free zone area of Alexandria, Egypt. The Company has invested $750,000 U.S. ($1,114,442 Cdn.), (December 31, 2003 - $675,000 U.S. ($1,014,264 Cdn.) maintaining its 25% interest in this Egyptian company. The Company accounts for its investment in this Egyptian Company on the cost basis as it does not exercise significant influence. Earnings from the Company's Egyptian investment will be recognized only to the extent received or receivable. While management believes that the investment in the Egyptian company is fully recoverable, there could be future developments and additional information could become available that may indicate that the carrying value should be revised. Management believes that future revisions to the carrying value, if any, would not have a material adverse affect on the Company's financial condition. However, should such revisions be necessary, the amounts could be material to the results of operations for the period in which they are reported.

Pre–operating costs

Pre-operating costs represent the costs incurred during the start-up of the Company's Slave Lake fractionation plant. The pre-operating period ended January 1, 2003 and the costs are being amortized over a period of five years.

7. Bank indebtedness and Long-term debt

During the year ended December 31, 2004 the Company entered into a new $28,190,000 (December 31, 2003 - $16,819,000) credit facility with a Canadian chartered bank consisting of a $15,000,000 (December 31, 2003 - $10,000,000) demand operating loan that bears interest at the bank's prime rate plus 0.40%; a $1,000,000 (December 31, 2003 - $500,000) demand revolving loan at the bank's prime rate plus 0.90%; demand non-revolving loans totaling $7,190,000 (December 31, 2003 - $6,319,000) that bear interest at the bank's prime rate plus 0.90%; and, a $5,000,000 (2003 – NIL) bank guarantee facility that bears a fee of 1.35% per annum at the time of issuance of each bank guarantee under the facility. Non-revolving demand loans are repayable in blended monthly payments of $113,526 (2003 - $81,500) and mature at varying dates from May 2006 to May 2020. At December 31, 2004, $3,476,944 of the demand operating loan was drawn and financed through bankers' acceptances of $3,500,000 which bear interest at 4.37%.

The Company has pledged an assignment of accounts receivable and inventories, a general security agreement charging all present and after acquired equipment and demand collateral mortgages aggregating $1,475,000 on land and buildings as collateral on the demand revolving and non-revolving loans.

While the credit facility is demand in nature, repayment of the debt in advance of the agreed terms is not at the bank's discretion provided the Company is not in default of its obligations, covenants and other conditions to the facility that will materially affect the Company's ability to fulfill its obligations. The Company was in compliance with these covenants at December 31, 2004.

	December 31, 2004	December 31, 2003
	$	$
Demand non-revolving loans	4,215,721	2,819,331
Less: current portion of long-term debt	1,173,087	846,565
	3,042,634	1,972,766

Approximate principal repayments in each of the next five years are as follows:

	$
2005	1,173,087
2006	1,234,907
2007	422,414
2008	320,685
2009 and thereafter	1,064,628

8. Asset retirement obligations

All legal obligations for the retirement of long-lived assets were identified and the fair value of these obligations was determined as of December 31, 2004. Upon the adoption of the new standard, the Company recorded the current fair value of its expected cost related to the asset retirement obligation (ARO). The analysis of the ARO for the year ended December 31, 2004 is as follows:

	$
Initial ARO on adoption of the new standard	137,261
Accretion expense	32,059
Balance as at December 31, 2004	169,320

Included in depreciation and amortization of plant and equipment is a charge of $39,400 for the amortization of the ARO. With the adoption of this standard, $137,261 has been included in property, plant and equipment.

The following assumptions were used to estimate the fair values of the obligation on the date the obligation was incurred:

Total undiscounted amount of the estimated cash flows	$1,186,000
Expected timing of payment of cash flows	2033 and 2041
Credit adjusted risk free rate	6.49% and 6.87%

The provisions of this section require that the standard be applied retroactively with restatement of comparative periods. The Company has elected not to restate its comparative periods as the amount required for restatement was not material.

The estimate of the total liability for future asset retirement obligations is subject to change based on amendments to laws and regulations and as new information concerning the Company's operations becomes available. Future changes, if any, to the estimated total liability as a result of amended requirements, laws, regulations and operating assumptions may be significant and would be recognized prospectively as a change in estimate, when applicable.

9. Obligations under capital leases

Obligations under capital leases are repayable in blended monthly payments of $7,500 to July 31, 2004. The Company has purchased the land and building comprising the obligation under capital lease for $875,000 on August 1, 2004. The future minimum lease payments under capital leases amount to $nil (December 31, 2003 – $927,500) and are as follows:

	December 31, 2004	December 31, 2003
	$	$
2004	-	927,500
Total minimum lease payments	-	927,500
Less: amount representing interest at 4.6%	-	23,985
Balance of obligation	-	903,515
Less: current portion of obligations under capital leases	-	903,515
	-	-

During the year ended December 31, 2004 the interest portion of lease payments amounted to $23,985.

10. Share capital and Contributed surplus

(a) **Authorized** -

20,000,000 non-voting, preferred shares, rights to be determined upon issue
Unlimited number of common shares

(b) **Issued** -

Common

	December 31, 2004		December 31, 2003	
	#	$	#	$
Balance - beginning of period	14,317,655	26,769,227	14,041,873	26,019,858
Issue of shares for cash upon exercise of stock options	138,000	272,900	161,700	336,655
Issue of shares for cash through employee share purchase plan	138,955	423,844	14,082	412,714
Balance - end of period	14,594,610	27,465,971	14,317,655	26,769,227
Contributed Surplus	-	591,431	-	298,087

(c) **Stock options**

The Company has reserved 2,700,000 common shares for issuance pursuant to an approved stock option plan ("Option Plan") granted to directors, management and employees of the Company. Stock options granted to employees vest after varying terms and amounts from the date of grant and expire five years after the date of grant. The exercise price of each option equals the market price of the Company's common shares at the date of grant. A summary of the status of the Company's Option Plan is presented below:

	December 31, 2004		December 31, 2003	
	Options	Weighted Average Excercise Price	Options	Weighted Average Excercise Price
	#	$	#	$
Common shares under option-beginning of year	1,214,000	2.94	1,677,000	2.94
Share options granted	160,000	3.49	35,000	3.57
Share options cancelled	(10,000)	5.15	(50,000)	3.38
Share options expired	-	-	(286,300)	4.73
Share options exercised	(138,000)	1.98	(161,700)	2.08
Common shares under option-end of year	1,226,000	3.11	1,214,000	2.94
Options exercisable at end of year	956,000	2.66	994,000	2.49

The following options were outstanding and exercisable under the Option Plan at December 31, 2004:

	Outstanding				Exercisable	
		Exercise Price				
Expiry Date	Options	Price	Weighted Average Price	Weighted Average Remaining Years of Contractual Life	Options	Weighted Average Exercise Price
	#	$	$		#	$
January 28, 2005	364,000	1.95	1.95	0.1	364,000	1.95
January 4, 2006	50,000	2.95	2.95	1.1	50,000	2.95
April 17, 2006	432,000	3.04	3.04	1.3	432,000	3.04
May 9, 2007	185,000	5.15	5.15	2.3	-	-
February 11, 2008	15,000	4.00	4.00	3.2	5,000	4.00
August 8, 2008	20,000	3.25	3.25	3.7	5,000	3.25
January 20, 2009	10,000	3.40	3.40	4.1	-	-
January 20, 2009	100,000	3.40	3.40	4.1	100,000	3.40
May 14, 2009	50,000	3.70	3.70	4.4	-	-
	1,226,000		3.11	1.5	956,000	2.66

10. Share capital and Contributed surplus (continued)

(c) Stock options (continued)

During the year ended December 31, 2004, the Company granted 160,000 options (December 31, 2003 – 35,000) with an exercise price ranging from $3.40 to $3.70 (December 31, 2003 - $3.25 to $4.00). The fair value of the options granted for the year ended December 31, 2004 has been estimated using the Black-Scholes option pricing model. The assumptions used in the pricing model are as follows:

Risk free interest rate (%)	3.69 and 4.00
Expected life of options (years)	5
Expected volatility (%)	53
Dividend yield (%)	0

The impact of expensing the stock options for the year ended December 31, 2004 was $293,345 (December 31, 2003 - $163,300), with a corresponding increase in contributed surplus. In addition, opening retained earnings have been restated at January 1, 2003 by $134,787 to reflect stock based compensation costs associated with the Company's 2002 fiscal year.

Under the Employee Share Purchase Plan ("Plan") an aggregate of 970,000 common shares have been reserved for sale to employees of the Company. Employees electing to participate in the Plan may contribute a minimum of two percent to a maximum of five percent of monthly salaries. The employees' contributions are matched equally by the Company. The share purchase price is equal to the weighted average of the trading prices of the common shares of the Company on the Toronto Stock Exchange for the five days on which the shares traded on or before the last day of the month for which contributions were remitted. Common shares acquired under the Plan vest with the employee upon purchase and are distributed to the employees on an annual basis. The Company's contributions to the Plan are recorded as compensation costs in the month incurred and totaled $211,922 for the year ended December 31, 2004 (December 31, 2003 - $206,357). During fiscal 2004, 138,955 shares (December 31, 2003 - 114,082) were issued under the plan for proceeds totaling $423,844 (December 31, 2003 - $412,714).

(d) Net earnings per share

Basic earnings per share is calculated using the reported net earnings divided by the weighted average number of common shares outstanding during the period. Diluted earnings per share is calculated on the basis of the weighted average number of common shares outstanding recognizing the effect of outstanding stock options and their equivalent using the treasury stock method.

A reconciliation of the denominators used for the computation of basic and diluted per share are as follows:

	December 31, 2004	December 31, 2003
	$	$
Weighted average share reconciliation		
- Basic		
Common shares - opening	14,317,655	14,041,873
Weighted average of common shares issued during the period	79,156	199,887
	14,396,811	14,241,760
- Diluted		
Basic weighted average common shares - opening	14,396,811	14,241,760
Dilutive effect of stock options and equivalents	186,421	-
	14,583,232	14,241,760

Diluted loss per share from continuing and discontinued operations are anti dilutive for 2003.

11. Interest expense

Interest expense is comprised as follows:

	December 31, 2004	December 31, 2003
	$	$
Interest on bank indebtedness	140,953	145,760
Interest on capital leases	23,985	42,863
Other interest	29,879	20,921
Interest on long-term debt	130,737	177,187
	325,554	386,731

12. Income taxes

The following table reconciles income taxes from operations calculated at the combined statutory federal and provincial tax rate with the income tax provision in the financial statements.

	December 31, 2004	December 31, 2003
	$	$
Income taxes based on combined statutory Canadian federal and provincial tax rate	1,061,432	(67,361)
Substantively enacted rates	(37,058)	(20,242)
Tax authority reassessments	-	57,970
Capital tax	-	71,663
Non-deductible (taxable) and other	148,765	(20,030)
	1,173,139	22,000

	$	$
Cash income taxes paid (received)	76,577	(1,201,035)

Significant components of the Company's future tax liabilities (assets) are as follows:

	December 31, 2004	December 31, 2003
	$	$
Property, plant and equipment	2,879,475	2,330,027
Non-capital losses	(497,036)	(1,127,741)
Other assets	102,365	132,579
Accounts payable and accrued liabilities	(84,050)	(86,550)
Asset retirement obligation	(56,925)	-
Share issuance costs	(135,190)	(212,815)
	2,208,639	1,035,500

As at December 31, 2004, the Company had approximately $1,478,000 (2003 - $3,258,000) of non-capital losses, subject to confirmation by income tax authorities, available to reduce future years' income for tax purposes. The non-capital losses will expire in 2010.

13. Supplementary cash flow information

	December 31, 2004	December 31, 2003
	$	$
Cash interest income received	3,687	26,379
Cash interest expense paid	279,383	409,956

14. Changes in non-cash components of working capital

Changes in non-cash components of working capital are comprised as follows:

	December 31, 2004	December 31, 2003
	$	$
Net change in accounts receivable	(5,541,402)	(1,744,515)
Net change in inventories and prepaid expenses	(1,496,845)	(1,630,452)
Net change in accounts payable and accrued liabilities	4,847,830	2,013,093
Net change in income taxes payable	(137,222)	1,323,512
	(2,327,639)	(38,362)

15. Commitments

(a) Leases

The future minimum lease payments under operating leases amount to $891,715 (December 31, 2003 - $741,425) and for each of the next five years are:

	$
2005	680,955
2006	192,981
2007	17,779
2008	-
2009	-

(b) Letters of guarantee and credit

The Company had provided a $408,000 U.S. ($525,055 CDN) letter of guarantee in favour of the Egyptian Gulf Bank on behalf of the Egyptian Canadian Company for Chemicals Industries - F.Z. for bank loans advanced to that company. The Egyptian Gulf bank terminated its requirement for a letter of guarantee on February 28, 2003.

At December 31, 2003 the Company had provided a $1,000,000 letter of guarantee terminating May 2004 in favour of a supplier for ongoing purchases of petroleum feedstock from that company.

At December 31, 2003 the Company had provided a $500,000 letter of guarantee terminating December 2004 in favour of a financial institution as security for the Company's energy price hedging commitments.

(c) Petroleum feedstock

The Company has entered into contracts of varying terms and quantities for the purchase of petroleum feedstock for processing. These contracts are not speculative.

(d) Chemical purchases

The Company has entered into a two year chemical purchase contract effective December 1, 2003 with a U.S. based private company guaranteeing that the Company will purchase chemicals at market prices in amounts no less than $500,000 U.S. ($600,150 CDN) in each of the next two years.

16. Contingent liabilities

In the normal course of business, the Company is party to various claims and legal proceedings. While the final outcome with respect to the claims and legal proceedings pending, as at December 31, 2004, cannot be determined with certainty, it is the opinion of management that their resolution will not have a material adverse effect on the Company's financial position or results of operations.

17. Segmented information

During 2004, the Company's services were diversified with the establishment of its Energy Marketing Group. This diversification was precipitated to maximize value received by the Company for its hydrocarbon by-products, mitigate the Company's exposure to the seasonality of its operations and to provide energy marketing management and expertise. As a result, the Company's activities are divided into two distinct business segments: Oilfield Services, which represents the manufacture and sale of specialty chemical and hydrocarbon products, and Energy Marketing, which represents the purchasing, gathering and marketing of crude oil for resale to refiners and other customers.

December 31, 2004

	Oilfield Services	Energy Marketing	Consolidated
	$	$	$
Revenues	65,880,660	14,951,954	80,832,614
Cost of Sales	47,581,201	13,627,821	61,209,022
Gross Profit	18,299,459	1,324,133	19,623,592
Depreciation and amortization	1,930,972	-	1,930,972
Interest expense	325,554	-	325,554
Earnings from operations	2,059,405	1,000,722	3,060,127
Other income	73,712	-	73,712
Income taxes	1,173,139	-	1,173,139
Net earnings	959,978	1,000,722	1,960,700
Total Assets	58,799,616	2,853,610	61,653,226
Capital expenditures	3,253,368	-	3,253,368
Goodwill	6,049,530	-	6,049,530

During 2004, the Energy Marketing segment had sales to one customer accounting for approximately 98% of total revenues provided by this segment.

During 2003, the Company sold all of the issued and outstanding shares of its wholly-owned U.S. subsidiary company to a private company based in Midland, Texas (refer to note 3).

Corporate Governance

Full disclosure with respect to the Toronto Stock Exchange Corporate Committee requirements is contained in the Information Circular of Enerchem International Inc., prepared for the Annual General Meeting to be held May 19, 2005.

The main corporate governance practices followed by Enerchem involve the assumption by the directors of responsibility for stewardship of the Company. Enerchem's Board of Directors comprises seven members, six of whom qualify as unrelated directors by virtue of their independence from management or any interest, business or other relationship that could materially interfere with the directors' ability to act in the best interests of the Company. The Board of Directors has three committees being: the Audit Committee, the Compensation Committee and the Environmental Committee.

Enerchem is committed to the objectives of the corporate governance policy established by the Toronto Stock Exchange and will continue to work toward complying with the objectives set forth therein.

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Chairman of the Board
Director

Douglas F. Robinson
President and Chief Executive Officer
Director (3)

Kenneth A. Klein, B. Comm.
Director (1), (2)

William D. Burch, FCA
Director (1)

Hugh L. Planche
Director (2)

David F. Potter
Director (1), (2)

Kevin M. Maguire, P.Eng., MBA
Director (1)

Officers

Douglas F. Robinson
President and Chief Executive Officer (3)

Brian M. Zubach, CMA
Chief Financial Officer

J. Barrie Brookman
Vice President, Corporate Development (3)

Member of:
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(2) Compensation Committee
(3) Environmental Committee

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Legal Counsel

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Stock Exchange Listing

Toronto Stock Exchange: trading symbol "ECH" United States - Over the Counter 12g-3-2(b)

Shareholder information

Shareholders may obtain copies of annual and quarterly reports, news releases, product information and other Company information by contacting:

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